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COLORADO DEPARTMENT OF REVENUE
1375 Sherman St. Denver, CO 80203

Annual Report

for July 1, 1987
to June 30, 1988

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Vol. 1 - Director's Briefing

Report of the Executive Director

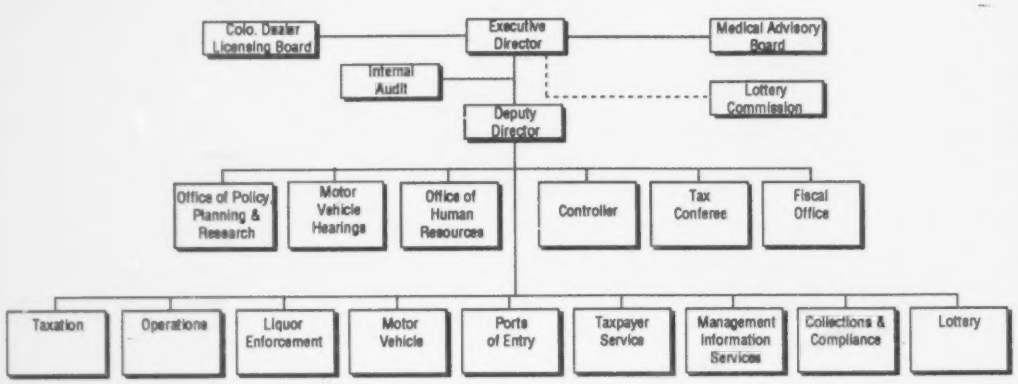
The 1987-88 fiscal year was one of challenge and change for the Colorado Department of Revenue. Implementation of the Tax Equity Act of 1987 was the focus of the first half of the year, while a comprehensive effort to improve organizational efficiency and effectiveness was the focus of the remainder of the year. Department employees succeeded in both endeavors, and, as this report shows, fulfilled all other responsibilities assigned to them by law or directive.

I am pleased, therefore, to present the forty-seventh annual report of the Colorado Department of Revenue. The report, which covers the period between July 1, 1987 and June 30, 1988, is submitted to the Governor and the General Assembly in accordance with C.R.S. 24-35-102(3).

Respectfully,

John J. Tipton
Executive Director

"For many citizens in this state, dealing with Department of Revenue employees may be the only contact they have with state government. Citizens meet you when they receive their driver's license, when they register to vote at a motor vehicle office, when they start a business, and when they file their annual income tax returns. You provide the example of how state government operates. The Department has performed its duties efficiently and effectively in the past. Yet I think it is admirable for employees to set their sights even higher — on a goal of excellence." — Governor Roy Romer, Letter to Revenue



Colorado Department of Revenue

Revenue employees were challenged to pursue two major goals in the 1987-88 fiscal year:

To make the department a pacesetter for quality and excellence in government.
To make the department a model of efficiency and innovation.

Employees in all divisions and at all levels rose to meet the challenge of these ambitious goals with impressive results.

The most visible result was successful implementation of the historic Tax Equity Act of 1987. Also known as the "single-rate" or "flat tax" bill, the new law enabled the department to create a simple 10-line form that could be used by more than 80 percent of the 1.7 million people who file Colorado individual income tax returns. And while the public marveled over the ease of filing the new form, hundreds of Revenue employees worked behind the scenes to rewrite computer systems and establish procedures for processing the new forms.

Less visible but equally important was the completion of the Motor Vehicle Division's Distributed Data Processing (DDP) System. All of the state's 63 counties are now connected to this centralized computer network. DDP gives counties and law enforcement officials the ability to instantaneously update and retrieve the 10 million motor vehicle title and registration records processed each year. This massive system — which encompasses 95 computers, 500 video display terminals and 250 printers — was put into place within budget and ahead of schedule, earning the department an award from the National Association for Information Systems.

The department won a national award for its Distributed Data Processing System which is a computer network that centralizes motor vehicle records from all 63 counties.

For the fifth consecutive year, the department's Fair Share program generated more than $10 million in revenue collections through innovations in detecting tax evasion.

The Colorado Lottery distributed $33 million in proceeds to the Capitol Construction Fund, the Conservation Trust Fund and the Colorado Division of Parks and Recreation.

In addition to being a year of challenge, fiscal year 1987-88 was also a year of change. In January, the department bid farewell to Acting Executive Director Steven V. Berson, who was appointed Executive Director of the Department of Regulatory Agencies after 12 years with Revenue, and welcomed John J. Tipton as Revenue's new Executive Director.

Executive Director John J. Tipton and Deputy Director Amelie Buchanan .

Where excellence adds up

"The mission of the Department of Revenue is to provide meaningful programs which emphasize excellence, maximize revenues, provide essential services to our customers, provide a healthy and challenging work environment for our employees and are accomplished in the most cost effective and productive way possible." — Colorado Department of Revenue Mission Statement, April 1988

Executive Director John J. Tipton brought to the department a philosophy of excellence, productivity, incentive and innovation. These values were translated into a strategic plan for the department which has come to be known as the Two Year Plan. The plan sets specific goals for the next two fiscal years and was presented to employees at a series of employee meetings.

During the 1988-89 fiscal year, the department will analyze the efficiency and effectiveness of every program it administers. It will also establish performance standards and measurements for all its activities. And, in the process, each division will identify cost savings of at least two and one-half percent within its budget. An additional two and one-half percent savings will be identified in the second year of the plan, fiscal year 1989-90, bringing total savings to five percent over the life of the plan.

The most important feature of the Two Year Plan will be the reinvestment of these productivity savings in innovations that improve efficiency and the quality of services. The net result will be the introduction of new technologies and services at little or no additional cost to the taxpaying citizens of the state. Additionally, employees will see the benefits of their savings being reinvested in work method improvements that benefit both citizens and employees.

Already in place is the system and training manual that will be used for the program analysis phase, materials developed in-house by the Office of Policy, Planning and Research. The department with support from local law enforcement, local government and industry groups also secured an agreement with the legislature that allows the department to pilot test the concept behind the Two Year Plan. Under the agreement, on July 1, 1988 the department will be allowed to reinstate 10 liquor enforcement agents, who were laid off as a result of 1987-88 budget cuts, the cost of which will be covered by savings within the department's existing budget.

Liquor on which the required taxes have not been paid as well as illegal gambling devices are among the property confiscated by Liquor Enforcement agents. The state's enforcement program is especially important to small local jurisdictions who lack the resources to conduct comprehensive (and often undercover) liquor code violations.

Under the Two Year Plan, the department has also continued and enhanced a number of initiatives started before Mr. Tipton's appointment.

In October 1987, a comprehensive Quality and Excellence Program was initiated as a means of creating a cultural climate for achievement within the department. Components of the program included:

Selection of a quality and excellence theme by employees: "Colorado Department of Revenue Where Excellence Adds Up." A logo was created to illustrate and promote the theme in publications and at employee activities.

The Employee Suggestion Program to tap the creativity of all employees with a commitment to objectively evaluate and respond to each and every idea submitted, as well as to recognize and reward those that are implemented.

The Quality Improvement Process (QIP) which the Operations Division initiated in the 1986-87 fiscal year and was introduced in the Collection and Compliance Division in 1987-88. QIP consists of establishing statistical analyses of all tasks and processes performed by a work unit to provide ongoing evaluations of performance that can be used to prevent errors and diagnose problems. Quality circles make up the other constituent part of QIP. The department's goal is to establish QIP in all divisions over the next few years.

The Excellence Award Program through which individuals and work units will be rewarded for excellence.

Each of these programs acknowledges the expertise and value of the individual employee, a theme which has continued under the Two Year Plan. All of the products of the Two Year Plan, including measurement systems, work method improvements and innovations, are being designed and produced by teams of employees within each division.

Data entry personnel were among hundreds of department employees who contributed to the successful implementation of the Tax Equity Act of 1987, the most significant reform to the state's income tax laws in more than 20 years.

Better communications increases compliance

Consistent with the department's emphasis on excellence is a customer-service orientation based on the assumptions that:

Voluntary compliance is more cost effective than forced compliance.

Better communications from the department will improve voluntary compliance.

Nowhere in the organization was the truth of these axioms better demonstrated than in the Port of Entry Division. During the 1987-88 fiscal year, division representatives attended more than 30 meetings with trucking industry groups throughout the state and committed to make available more general information about the laws and regulations that govern commercial transportation in Colorado. For example, the digest of state regulations for truckers was expanded to include safety information, clearance information and one-stop shopping information. More than 5,000 copies of the publication were distributed by port employees.

A companion activity was the implementation of a division policy that de-emphasizes the number of enforcement actions taken by Port officers and measures employee productivity by the quality of enforcement actions.

Additionally, the Port of Entry Division in cooperation with the Colorado State Patrol has created a higher level of uniformity in the Motor Carrier Safety Program in which commercial vehicles are inspected for safety.

Concurrent with Port of Entry efforts to improve relations with the trucking industry was a departmentwide effort to establish a "one-stop-shopping" site at which truckers could obtain information about all state trucking requirements. Previously, truckers had to contact several different agencies to operate in the state.

Without compromising its enforcement mission or other responsibilities, the Port of Entry Division addressed several industry concerns and established a new direction. One key to the effort was the introduction of four pieces of legislation — all of which passed — designed to simplify and create a greater degree of self-compliance in the industry. At the same time, Port employees achieved several notable increases in productivity, such as a 62 percent increase in commercial safety inspections and a reduction in clearance time from 75 seconds to 35 seconds for vehicles in full compliance with state requirements.

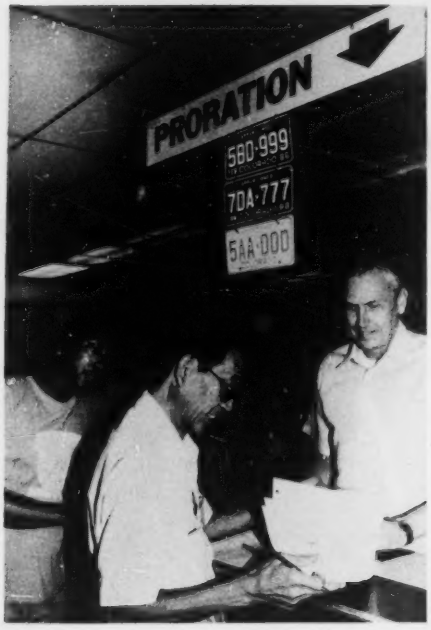
Mobile scales are an important component of the Port of Entry enforcement effort.

Similar communications efforts — large and small — were initiated in tax administration. The Taxpayer Service Division conducted the most ambitious income tax public information campaign ever concerning changes effected by the Tax Equity Act of 1987. A news conference was held to introduce the public to the new, simpler income tax return forms. In addition to issuing public service announcements and regular update news releases, the division also published 20,000 brochures that outlined the tax changes and distributed 11,000 tax preparer's handbooks.

Other new efforts focused on specific sectors of the taxpaying public who were affected by specific aspects of the tax reform law. For example, to reach members of the Public Employees Retirement Association (PERA), meetings were held with PERA officials to coordinate information distributed to members and a stuffer was included with state employee paychecks to notify them of tax law changes. A mini-campaign targeted senior citizen publications to explain reporting of retirement benefits. A "Tax Practitioners' Hotline" was established to make sure that practitioners, who prepare hundreds of returns each, got quick, accurate answers to their questions.

Revenue employees answered more than half a million telephone calls from taxpayers.

An example of a smaller communication effort was the Collection and Compliance information and enforcement campaign directed toward flea market vendors. With assistance from Taxpayer Service personnel, the division distributed information packets to flea market vendors statewide and conducted a news media campaign to enlist public support for state requirements that flea market vendors collect sales tax just like other retailers. Follow-up visits to flea markets, which were conducted after a "grace" period to allow vendors to comply, netted $3,790 in license fees from vendors not previously licensed plus $25,000 in additional sales tax from these new accounts.



The department opened a Motor Carrier Services Center at which truckers can obtain all state tax and regulatory information at one location. Before establishing this "one-stop-shopping" site, truckers had to contact several different state agencies.

Tax simplification improves public perception

"It was so simple, I thought part of it was missing," said one taxpayer of the 1987 state return form.

"I paid more this year, but I think the flat rate is fair," said another.

The Tax Equity Act of 1987 made sweeping reforms to Colorado's income tax laws that significantly streamlined filing requirements for taxpayers. The foundation of the tax reform law was a single or "flat" income tax rate for all individuals and the elimination of many state modifications to federal taxable income.

The rate of five percent meant many Coloradans would pay more state income tax than in previous years to compensate for recession-driven drops in state revenue from other sources. But by increasing the personal exemption and standard deduction amounts to match federal levels, the new law decreased taxes paid by low-income residents.

Overall public response to state tax reform was generally positive, particularly toward the simpler, shorter income tax returns. The short form 104A was reduced to 10 lines from 22 lines the previous year. The number of lines on the long form 104 was reduced to 32 from 64 the previous year. Designed in-house for the first time by Graphic Arts Section staff on desktop publishing computer equipment, the 1987 forms featured brighter colors, bigger type and bold graphics to enhance the ease of completing the forms. The new design also decreased printing and postage costs by decreasing the number of pages in the income tax booklet from 24 to 16.

Focus group studies conducted by independent researchers showed that taxpayers greeted the changes favorably.

Major revisions to the income tax computer program were needed to implement the Tax Equity Act of 1987.

Concluded on researcher's report: "Overall, it appears that the revisions to the booklet have indeed been effective in providing an image of an easier, less intimidating, process than in the past, and this image translates to a more positive attitude toward the Department as a whole.

The Liquor Enforcement Division revised its regulations under the Colorado Beer and Liquor Codes to simplify liquor excise tax reporting.

In an effort to simplify sales tax reporting, ongoing liaison work continued between the department and local government officials to increase uniformity between state sales tax requirements and those of Colorado's home rule cities. One formidable accomplishment was the adoption of new regulations governing the exemption of food from sales tax. These regulations went into effect in October 1987 and are now in use by all Colorado jurisdictions that exempt food from sales tax.

Other fiscal year 1987-88 accomplishments

After 10 years of case preparation and courtroom work, the department won a precedent-setting case concerning the computation of corporate income taxes on apportioned income from Colorado sources. The department successfully defended the inclusion of a corporation's worldwide operations in the Colorado base. Although statutory changes now allow the exclusion of most of this type of income from Colorado taxation, the case protected more than $50 million in corporate tax revenues.

The Collection and Compliance Division established a bankruptcy unit and streamlined the process for filing motions for dismissal and reliefs from stay. The unit collected $1.6 million during the fiscal year.

The Colorado Lottery, which celebrated its fifth anniversary, achieved sales of $90,944,020. The state legislature enacted legislation that authorized the start of a new Lotto game during the 1988-89 fiscal year. In Lotto, players will win prizes if numbers they select match numbers randomly drawn each week by the Lottery.

New automation initiatives in the Office of Policy, Planning and Research also enabled the department to provide statistical information to elected officials and the public in a more timely manner and to take a more active role in improving the accuracy of the state's revenue forecasts.

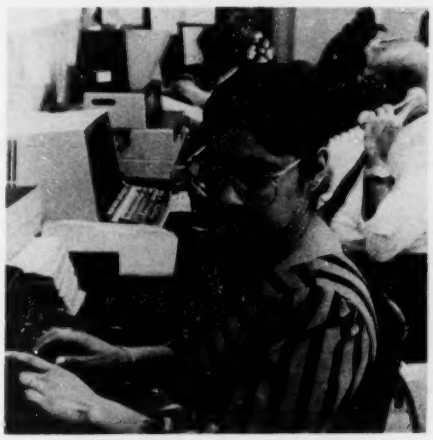
The Lottery invited the public to join its fifth anniversary

The Taxpayer Service Division combined organizational efficiency with community service through a program that provides college students from Metropolitan State College academic credit and "hands-on" tax experience. In return, each student must perform 150 hours of volunteer work for the department. The program, which began with eight students during the income tax filing season, was so successful that it will be conducted year-round.

Improvements and automation of information matching projects, such as those that compare information on federal tax returns with information on state tax returns, contributed to the ongoing success of the Fair Share program.

The Taxation Division's Criminal Tax Enforcement Unit launched a Misdemeanor Prosecution Program directed toward individuals who willfully fail to file state tax returns. Seven individuals have been referred for prosecution under the program. Other criminal enforcement activity includes case work that resulted in conviction of nine individuals for fraudulently obtaining special credits intended for low-income senior and handicapped citizens, as well as conviction of five contractors who illegally failed to pay employer taxes.

The Taxation Division generated $5.4 million in collections as a result of office audits by 7.5 tax examiners for an average of $720,000 per examiner.



For the fifth consecutive year, Fair Share employees generated more than $10 million in revenue.

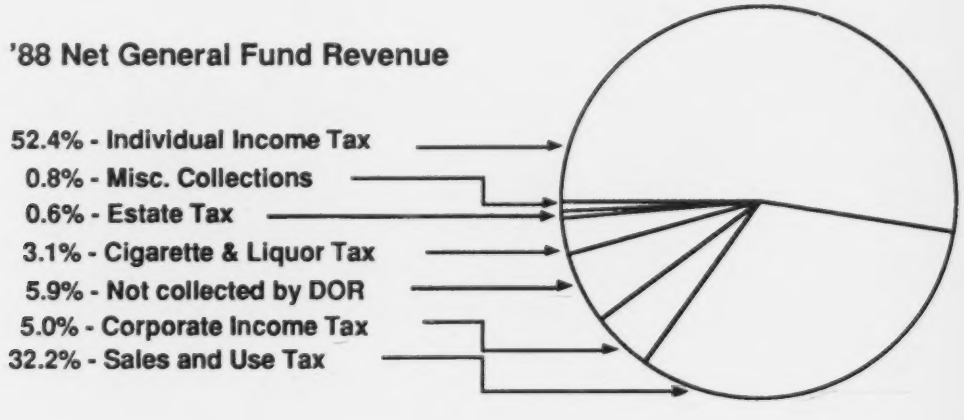
Collections, refunds & administrative costs

Refunds and Net Collections by Source

Fiscal Year Ended June 30, 1988

Taxes	Gross Collections	Refunds	Net Collections
Property:			
Motor Vehicle Specific Ownership 'A'	$5,926,029.44	$6,038,731.51	$(112,702.07)
Sales, Use, Excise and Gross Receipts:			
Alcoholic Beverages	$ 21,979,199.60	$14,506.16	$21,964,693.44
Tobacco Products Tax	3,104,098.38	727.77	3,103,370.61
Cigarette Tax	61,490,903.06	17,789,713.55 1/	43,701,189.51
General Sales	666,620,543.62	1,805,956.83	664,814,586.79
Use Tax	59,898,357.74	613,382.93	59,284,974.81
Tourism Promotion	6,776,057.69	18,286.41	6,757,771.28
Fuel Taxes	306,194,635.66	4,090,916.21	302,103,719.45
Subtotal	$1,126,063,795.75	$ 24,333,489.86	$1,101,730,305.89
Income Tax:	$1,568,464,732.15	$260,459,342.31	$1,308,005,389.84
Estate Tax:	$14,067,620.63	$894,217.95	$13,173,402.68
Severance Taxes:	$ 26,165,782.62	$10,836,237.22	$15,329,545.40
Gross Ton Mile:	$32,380,182.91	$1,343,548.14	$31,036,634.77
Licenses, Permits and Fees:			
Motor Vehicle Licenses	$ 32,129,114.24	$ 98,219.19	$ 32,030,895.05
Emissions	5,001,348.75	29,511.21	4,971,837.54
Motor Vehicle Titles	3,381,776.43	456.00	3,381,320.43
Subtotal	$ 40,512,239.42	$127,186.40	$40,385,053.02
Motor Vehicle Operators:	$5,412,655.52	$ 1,564.00	$ 5,411,091.52
Regulatory and Business:	$11,391,130.50	$16,247.25	$11,374,883.25
Other Receipts:			
Regional Transportation District	$78,340,000.76	$ 78,038,818.58	$ 301,182.18
City Sales Taxes	64,744,706.59	64,929,684.12	(184,977.53)
County Sales Taxes	69,290,365.72	67,104,236.28	2,186,129.44
All Other	14,930,819.37	7,205,793.07	7,725,026.30
Subtotal	$ 227,305,892.44	$217,278,532.05	$10,027,360.39
Total	**$3,057,690,061.38**	**$521,330,096.69**	**$2,536,359,964.69**

1/ Includes $17,029,504.09 distributed to cities and counties.


'88 Net General Fund Revenue
52.4% - Individual Income Tax
0.8% - Misc. Collections
0.6% - Estate Tax
3.1% - Cigarette & Liquor Tax
5.9% - Not collected by DOR
5.0% - Corporate Income Tax
32.2% - Sales and Use Tax